ComEd Ex. 8.0

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

COMMONWEALTH EDISON COMPANY,

Application for transitional funding order pursuant to Section 18-103 of the Public Utilities Act, approval of transactions with affiliates pursuant to Sections 7-101, 7-102 and 7-204A, and approval of an instrument funding charge tariff.

No. 98-0319

REBUTTAL TESTIMONY OF WILLIAM A. ABRAMS
PRESIDENT - WM. A. ABRAMS COMPANY

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REBUTTAL TESTIMONY OF WILLIAM A. ABRAMS
<u>PRESIDENT - WM. A. ABRAMS COMPANY</u>

Q. What is your name and business address?

A. My name is William A. Abrams, and my business address is 550 Frontage Road, Northfield, Illinois.

Q. Please state by whom you are employed and in what capacity, and briefly describe your educational background and business experience.

A. My occupation, educational background, and educational experience are summarized on Attachment 8.1.

Q. What is the purpose of your testimony in this proceeding?

A. I have been asked by Commonwealth Edison Company (ComEd) to testify as to how asset-backed securities (the "Notes") are likely to be reflected for credit rating purposes and the implication thereof. In addition, specifically, I am responding to

Mr. Rungren's conclusion that the Notes will be viewed as debt of ComEd and as an increase to ComEd's risk.

Q. Would you please summarize your conclusions?

A. Yes, I will do so in outline form referencing the highlights of my testimony as follows:

> The Notes are non-recourse to ComEd. These securities will be treated as off-balance sheet financing by the credit rating agencies. Therefore, it will not be counted by the agencies in evaluating ComEd's financial risk.
>
> The Notes add no bankruptcy risk as they will have no call upon the assets of ComEd, but only upon the intangible transition property created by statue and conveyed to the Note Issuer.
>
> Risk attached to the debt and to the common equity of ComEd also will be reduced by retirement of mortgage bond debt and by lower total debt recognized as "on-balance sheet" by the rating agencies.
>
> No additional risk to ComEd's common equity is perceived as a result of the Note sale. In fact, equity risk and total risk are expected to decline, reducing ComEd's total cost of capital.

Q. Mr. Abrams, are you aware that Ms. Ruth Ann M. Gillis has testified that the four major credit rating agencies have indicated that they will treat Notes as off-balance sheet financing for the purpose of credit ratings on ComEd's debt?

A. Yes, Ms. Gillis so indicated on page 43 of her initial testimony.

Q. Are the credit rating agencies likely to consider the Notes as off-balance sheet financing?

A. Yes. Where the securities are non-recourse to the company and the terms and conditions of the State legislation creating the structure for the issuance of Notes sufficiently separates the Notes from any claim on the assets of the issuing company, they would be considered an "off-balance sheet financing" for credit rating purposes. Under these circumstances, the agencies have determined that the securities do not have a negative impact on the credit rating of the originating company. In the case of ComEd, the Illinois enabling legislation appears to have made this separation. I understand that the financings completed by the three investor-owned California utilities, which are similar to the subject transaction, were treated as off-balance sheet for credit rating purposes. Similar types of adjustment are regularly made where necessary to properly show the company's "numbers" in isolation and in comparison with the universe of companies with which the subject company is to be compared. In all cases, the effort is to present data that reflects economic reality rather than an accounting formula.

Q. Has any rating agency issued a policy statement about securitization, the balance sheet ratios, interest burden, and credit ratings?

A. Yes, for example, DCR, in July 1997, published its opinion of and method of handling securitization in "DCR's Views on Securitization Financings of Stranded Cost Recovery Revenues". This is included as Attachment 8.2.

I will paraphrase from Attachment 8.2 key items relevant to this proceeding.

> Securitized financings would improve the risk profile and credit quality of the utilities that accomplish them.
>
> The utilities will have no responsibility for payment of the interest or principal on the securitized debt.
>
> The SEC-required accounting treatment, i.e., treating the securitized debt as on-balance sheet, will give the appearance of higher debt leverage and increased interest expense burden suggesting a utility with a weakened financial condition and lower credit quality. In reality, quite the opposite will result.
>
> Accounting treatments do not always reflect a transaction's economic substance and legal characteristics.

> When analyzed on this corrected basis--i.e., securitized debt treated as an off-balance sheet financing--utilities will have lower levels of debt obligations, lower interest burdens, and about the same leverage levels as prior to securitization.

Q. What is the effect of the agencies treating asset-backed securities as off-balance sheet financing?

A. There would be a reduction in the total amount of debt considered by the agencies in the credit rating process. The proceeds of the Notes would enable ComEd to retire higher cost conventional debt and reduce interest expense. To the extent that first mortgage debt is retired, junior debt would benefit without the strong claim of the mortgage bonds. The equity would benefit with a smaller amount of outstanding mortgage bonds with their special rights and privileges, especially in bankruptcy - however remote the possibility of bankruptcy might be.

Q. What is the ultimate effect upon ComEd of the agencies' actions to treat the Notes as off-balance sheet for credit rating purposes?

A. ComEd could receive a higher credit rating for its conventional debt and preferred stock than otherwise, all other factors equal. That would give ComEd a lower cost of conventional debt, and less perceived risk applicable to its common equity. In other words, ComEd would have less, not more, financial risk.

Q. Are the Notes as much of a burden, even if not separated on the balance sheet, as the other debt of ComEd?

A. No. First, unlike bank debt, payments of principal on the Notes may, by their terms, be deferred. Further, unlike mortgage bonds, the Notes do not encumber any physical assets of ComEd. This gives ComEd greater operational flexibility to maximize its profitability. Finally, unlike other securities, including debt which is often continually refinanced, the Notes will be paid in full within a relatively short time period. Thus, investors will view the Notes, unlike other securities, as a new type of transitional financing which will reduce financing costs.

Q. Do equity investors look to credit ratings in making their investment decisions?

A. Yes, many equity investors do so. Credit ratings are used regularly by equity investors to define and limit risk targets. Many investors will only buy equities of companies which are investment grade, i.e., BBB credit rating or above. Others will want "AA" companies. Some investors are restricted by regulation -- such as insurance companies, pension funds, etc. -- to securities of companies with a certain minimum debt rating.

Q. Would you expect ComEd's common equity cost to rise as a result of the issuance of the Notes and use of the proceeds as proposed by ComEd?

A. No, I would not. I would expect the cost of capital to decline for the following reasons:

- The Legislature appears to have carefully structured the framework for the Notes to compete for the highest credit rating to maximize the company's cost reduction which, in turn, leads to reduction in risk.

- Cost reductions should assist growth and enhance the ability to sell common equity in the future if necessary to support ComEd's business operations. This could add to credit quality and further reduce cost of capital.

Q. Does this conclude your testimony?

A. Yes.

EMPLOYMENT & BUSINESS EXPERIENCE
WILLIAM A. ABRAMS CFA

Wm. A. Abrams received a Bachelor of Science degree from Loyola University (Chicago, Illinois) in 1951, majoring in business administration. He is President of the Wm. A. Abrams Company, a financial consulting Firm formed in 1995.

From 1951 until 1967, he was engaged successively in industry, management consulting, and corporate finance. In 1967, he joined Duff & Phelps (D&P) as a senior financial analyst following industrial equities. D&P was then principally an investment research firm. From 1969 until 1980, his primary responsibilities had been to analyze the common equity and the debt of utility companies, and to make report-form and verbal buy-hold-sell recommendations to the D&P clients (principally institutional and large individual investors, and brokers). From 1974, he also was Chairman of D&P's Utility Fixed Income Rating Committee which was responsible for issuing private ratings on the fixed income securities.

Beginning in 1980 and through 1994, his responsibilities had been entirely with DCR, initially a subsidiary of D&P and later spun off. he was in charge of all electric, gas, and telecommunications credit ratings. He was successively promoted, ultimately to Senior Vice President and a member of the Executive Committee. Since 1995, he has been Executive Consultant to Management at DCR.

On the basis of his experience and a series of written examinations, he was awarded the professional designation of Chartered Financial Analyst by the Institute of Chartered Financial Analysts in 1971.

He is a member of the Association for Investment Management and Research, and of the Investment Analysts Society of Chicago, Inc.

He has testified before a number of regulatory commissions including: Arizona, California, Delaware, The District of Columbia, Georgia, Florida, Indiana, Kansas, Maine, Maryland, Michigan, Minnesota, Mississippi, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Texas, Washington, Wisconsin, and before the Federal Energy Regulatory Commission on rate of return, financing, accounting policies, factors affecting credit rating, customer contracts, firm purchased power contracts, and mergers.

He has lectured on rate regulation, utility financing and the analysis of public utility companies and their securities to classes of graduate students at Northwestern University and as guest faculty member for the Executive Development Center seminars sponsored by the University of Illinois and the University of Notre Dame. He consults with utility companies on financial matters and has been a guest speaker on financial integrity issues before utility boards of directors. He has given speeches and served on panels on utility matters before investor, utility and expert witness groups; the PUR Financial Conference; Edison Electric Institute conferences; the Iowa State University Regulatory Conference; Independent Power groups; Merrill Lynch Capital Markets seminars; Kidder Peabody Regulatory seminars; and the Society of Rate of Return Analysts. He has lectured before Eastern European government officials on privatization. He has authored articles on utility-related subjects for publication in "Credit Decisions," a weekly credit review published by DCR, and in "Electric Perspectives."